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Macroeconomic policy questions: commodities

World commodity trends and prospects

Note by the Secretary-General

The Secretary-General has the honour to submit to the General Assembly, as requested in its resolution 55/183 of 20 December 2000, the attached report,** which was prepared by the Secretary-General of the United Nations Conference on Trade and Development (see annex).

* A/57/150.
** The report was submitted late in order to ensure that the most recent statistics available could be used in its preparation.

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Annex

Report of the Secretary-General of the United Nations Conference on Trade and Development on world commodity trends and prospects

Executive summary

World exports of non-fuel commodities increased at a slower rate than total exports during the decade 1990-2000. The value of exports of agricultural commodities actually decreased from 1996 to 2000. Developing countries' share of world commodity exports increased slightly, although it is still below the levels reached prior to 1985. The share of African countries has continued to decrease. Dependence on exports of a few commodities remains high in a large number of developing countries. Prices of commodities have continued their downward trend, and the level of commodity prices in current United States dollars is now comparable with that of the early 1970s. Since 1997, the fall in prices of some commodities, including coffee, cotton and sugar, has been dramatic, causing large economic losses and increased poverty in several developing countries.

While the elimination of supply-side constraints are of fundamental importance, two major problems in the area of commodities require the urgent attention of the international community: the catastrophic price falls for some commodities and the continuation of agricultural support policies by developed countries. The international community should mobilize resources to finance the withdrawal of productive capacity for the commodities having experienced dramatic falls in prices. As a minimum, support schemes to developed-country producers competing with developing-country producers of the commodities concerned should be radically reduced, if not eliminated.

In the long term, developing countries need assistance in order to improve their supply capacity, the quality of their products and their participation in international value chains. Institutional factors such as insufficient market information, lack of access to technology and inputs, lack of extension services, difficult access to finance, and lack of organization and cooperation among domestic firms pose formidable barriers to the expansion of commodity exports and to diversification. Policy action in these areas, by individual Governments as well as the international community, with the active involvement of the private sector, can make a significant positive impact on the livelihood of developing-country commodity producers. Significant improvements in market access for developing-country agricultural exports require, apart from a sharp and meaningful reduction of subsidies, much deeper cuts in tariffs, or large increases in the volumes admitted at lower tariffs, preferably both. In this context, the burden of liberalization on net food-importing countries and specialized exporters that depend on one or two key commodities also needs to be addressed.

International producer-consumer cooperation should be supported and the activities of the Second Account of the Common Fund for Commodities (CFC) should be expanded. In particular, increased funding should be made available to CFC to finance research and development and extension services in developing countries.

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I. Recent developments in the world commodity economy

A. Commodity trade and production in developing countries

1. While total world exports increased at an average annual rate of 6.1 per cent between 1990 and 2000, world commodity exports grew by 3.1 per cent. Food exports peaked in 1996 at 468 billion United States dollars and declined every year thereafter, to 429 billion dollars in 2000. World exports of minerals and metals increased at a relatively stable average annual rate of 3.8 per cent during the period, while world exports of agricultural raw materials peaked in 1995-1996 and by 2000, had returned to a value slightly lower than that of 1990.[a] The share of developing countries in world food exports increased slightly from 29 to 32.4 per cent, although it was still below the 1985 level of 34.7 per cent. While developing countries in America and Asia increased their market shares, that of African countries decreased. With respect to minerals and metals, the pattern is similar, with a slight increase in the share of developing countries as a group, composed of a large increase for Asia, stagnation for America and a halving for Africa.

2. Differences in growth between commodities reflect changing consumer habits, with fast growth for items such as fish, fresh fruits and vegetables and tobacco, and slower growth for animal oils and fats, coffee and cereals. The growth in trade is affected by market access conditions and marketing and promotion efforts by exporters.

3. Since total exports by developing countries increased at an average annual rate of 9.3 per cent from 1990 to 2000, a rate faster than that for commodity exports, these countries as a group have become less dependent on commodity exports over the last decade. However, there are differences between countries. The number of developing countries that depend on primary commodities, excluding fuels, for more than half of their export earnings remained almost unchanged in 1999 from a decade earlier — 61 out of the 144 countries for which data were available. If fuels are included, the number rises to 88. Many countries also still depend on a very small number of commodities for export earnings: three or fewer commodities accounted for more than half of the total export earnings of 61 developing countries in 1990 and of 46 in 1999, of which 22 export mainly fuels.

4. Developing countries with more diversified export structures have generally experienced higher rates of economic growth than those depending on commodities. Nevertheless, exporting commodities, including more processed and higher-value items, may well be the most viable path to increasing incomes, employment and welfare for many countries. In several developing countries, such as Botswana, Chile, Malaysia and Thailand, growing export revenues from the commodities sector — as a result of a high rate of growth in world demand and/or the exploitation of competitive advantages — have provided the necessary resources for investment in both productive capacity and infrastructure, enabling those countries to enter new productive activities and thereby diversifying production and exports. On the other hand, several other countries, particularly least developed countries, have not succeeded in generating sufficient revenue from their commodity exports to allow diversification and growth, owing to combinations of demand factors (stagnating world demand, declining prices), unfavourable market access or market entry conditions, competition from subsidized production and supply-side bottlenecks.

B. Commodity prices

1. Evolution of commodity prices over the long term

5. The long-term trends in commodity prices reflect, apart from slow growth in demand, considerable increases in productivity. In competitive markets characterized by low price and income elasticities of demand, this leads to falling real prices, with the productivity gains being passed on to consumers. Prices are also influenced by other factors, such as subsidies, differences in bargaining strength between producers and consumers and excesses of supply over demand (due to exit barriers and inability to diversify production), all of which affect the distribution of productivity gains and have exercised a downward pressure on prices over long periods.

6. Over the past 25 years, from 1977 through 2001, the combined United Nations Conference on Trade and Development (UNCTAD) price index in United States dollars for all commodities declined by 53 per cent in

real terms,[b] that is to say, commodity prices lost more than half of their purchasing power in terms of manufactured goods. In current dollar terms, the index also declined, although by less (11 per cent), over the past quarter-century. The price falls were most serious for tropical beverages and for vegetable oilseeds and oils. Over the last decade, only vegetable oils and oilseeds showed a slight price increase. In nominal terms, the level of the commodity price index is now comparable with that of the early 1970s.

2. Recent commodity price falls

7. The last four years have seen an acceleration of the declining trend. Through May 2002, the combined price index for all commodities fell by 17 per cent in real terms and by 24 per cent in current dollars.[c] The fall has been precipitous for tropical beverages at 55 per cent in current dollars, with other agricultural commodity groups experiencing price falls of about 30 per cent and minerals and metals price falls of about 18 per cent. Prices of some commodities (cocoa, sugar, meats and rubber) decreased markedly from 1998 to 2000 but recovered in 2001-2002. Prices of metals and minerals depend strongly on world economic performance. While precious metals played their usual role of "safe havens", prices of non-ferrous metals such as nickel, aluminium, copper, zinc and tin plunged dramatically. Although base-metal prices recovered slightly in early 2002, owing to positive economic growth forecasts, the overall trend is still negative and market fundamentals do not give cause for optimism.

8. The sharp decline in United States dollar prices can be attributed to a number of factors, including dollar appreciation, currency devaluations of major commodity exporters and the general economic downturn. Other factors also contributed to the severity of the price declines. A structural oversupply can be observed in the case of some commodities such as coffee. This has been due mainly to production increases, particularly through the emergence of new producers, as well as productivity improvements, and a declining rate of growth in demand (or absolute declines: coffee consumption in the United States of America halved from 1960 to 2000). Market distortions are another explanation in the case of commodities such as cotton and sugar, which are produced in both developed and developing countries, and where countries having already liberalized their agricultural sectors have to compete with countries providing generous support to their agriculture.[d]

9. The recent commodity price falls have had a major impact on developing countries. Many of these countries are economically vulnerable and often have to face boom-and-bust situations. They have to deal with the risk of falls in foreign exchange earnings from commodity exports — which influence their capacity to import — and they are affected by rapid increases in prices of imported commodities such as oil. For instance, Ghana mainly exports cocoa and gold and imports oil. Between 1998 and 2000, prices of cocoa and gold fell by 47 and 5 per cent respectively, while oil prices increased by 116 per cent. The situation reversed itself in 2001-2002 with an estimated increase of 76 per cent in cocoa prices and a fall of 15 per cent in oil prices. Managing such cycles is a major macroeconomic task.

10. According to a rough calculation made by the UNCTAD secretariat, if, over the 1999-2002 period, the prices of coffee, sugar and cotton had remained at the level at which they were in 1998 (when they were, historically speaking, "average"), coffee producing countries, sugar producing countries exporting to the free market and West African cotton producing countries would have earned respectively 19 billion, 1.4 billion and 1 billion United States dollars more than they actually did earn.

11. The case of coffee is illustrative. About 70 per cent of the world's coffee supply is provided by smallholders who are directly affected by the price fall. For instance, coffee growing supports more than 40 per cent of the rural labour force in countries such as Nicaragua. According to calculations made by Oxfam,[e] farmers in the Dominican Republic growing coffee on two hectares earn only US$ 260 a year from coffee production. The collapse of the world price for coffee directly affects 125 million people who depend on it for their livelihoods. This is having catastrophic consequences in terms of increased poverty.

3. The gap between international and consumer prices

12. It is possible that the impact of oversupply and slow economic growth on commodity prices would be somewhat alleviated if price falls experienced by producers were reflected fully in prices paid by final consumers. However, as described in the report of

UNCTAD on world commodity trends and prospects (A/55/332) submitted to the General Assembly in 2000, declines in the prices received by producers appear to lead to higher profits at later stages of the value chain, before the product reaches the final consumer. In general, the stage in the processing chain where concentration is largest tends to acquire a large share, with other stages having to accept smaller portions of the final price. For instance, following recent falls in cotton prices, the difference between the International Cotton Advisory Committee (ICAC) price indices for cotton and cotton yarn in the growing season 2001/02 was the greatest since the yarn index had first been calculated in 1982.[f] According to the International Coffee Organization (ICO),[g] coffee producing countries received about US$ 10-12 billion out of a $30 billion retail market in the United States at the end of the 1980s. Today, while the value of retail sales exceeds $70 billion, they only receive $5.5 billion. On the other hand, price increases for the primary product may not always be accepted by later stages with a strong market position. Thus, it was reported that the cocoa processor Archer Daniels Midlands cut capacity at its processing plant in Côte d'Ivoire because "prices for cocoa beans had risen but chocolate makers were not paying more for processed products".[h] It should be noted, however, that other chocolate producers have raised their prices in response to the higher price for cocoa beans.[i]

II. International commodity markets

A. Developments in the world trading system

1. Agricultural protectionism and support

13. While the implementation of the commitments under the Uruguay Round of Multilateral Trade Negotiations Agreement on Agriculture[j] by developed countries was completed in 2000, agricultural tariffs in these countries have remained high. Average most-favoured-nation (MFN) agricultural tariffs in the Organisation for Economic Cooperation and Development (OECD) countries are about 60 per cent, whereas industrial tariffs are rarely above 10 per cent (other than for textiles and clothing).[k] Most of the tariff peaks are in agriculture, including processed products. Moreover, agricultural tariffs are sometimes very complex and include seasonal variations. In addition, the tendency for tariffs to escalate according to the degree of processing remains a major problem. With few exceptions, post-Uruguay Round tariffs escalate not only between raw and semi-finished but also between semi-finished and finished items, thus impacting on the more advanced stages of processing more strongly. This continues to pose impediments to developing countries' opportunities to increase exports of higher value added products such as those based on cocoa and coffee, canned fruits and vegetables and concentrated fruit juice. Finally, although developing countries have been accorded preferences under a multitude of agreements, exceptions to these preferences often relate to agricultural products. For example, the European Union (EU) initiative on "Everything but Arms" (EBA) offers free market access to products from the least developed countries, with less than 5 per cent of pre-EBA exports left facing a tariff barrier. According to simulations however, the impact of this initiative will be a relatively small increase in exports from the least developed countries in the medium term, as 70 per cent of the potential positive trade effects would have come from free access for sugar, rice and bananas, which has been deferred until 2006.[l]

14. Under the Agreement on Agriculture, developed countries also committed themselves to reducing certain types of support to agriculture considered to be trade distorting by 36 per cent in comparison with the reference period, 1986-1988.[m] Since the reference period was characterized by historically high levels of agricultural support, actual reductions in the last decade have not been significant. Moreover, the Agreement on Agriculture allows the continuation of supports judged to be less distorting (such as payments based on area planted or historical entitlements) at the same or higher levels than in the past. Such support measures, while not targeting prices or unit production costs, reduce the business risk for farmers and provide them with an incentive to continue or increase production, including for exports. Thus, although the most trade distorting measures, including direct export subsidies, have been somewhat reduced,[n] developed-country agricultural producers enjoy a competitive advantage.

15. In both 2000 and 2001, support to agricultural production (total support estimate (TSE) by OECD countries declined slightly to US$ 321 billion and US$ 311 billion respectively owing to increasing prices for supported products, and this resulted in lower price

support. Compared with the 1986-1988 level of $298 billion, TSE increased slightly, owing to increased spending on support measures that are not subject to Agreement on Agriculture reduction commitments.[o] Agricultural support in OECD countries continues to be about eight times as large as net transfers of official development assistance (ODA) to developing countries by the same countries (less than US$ 40 billion in 2000). On average in OECD countries, support to producers accounts for 31 per cent of total farm receipts, of which 78 per cent is in the form of market price support, output payments and input subsidies. Support levels differ between countries and commodities, with higher support being given to those producers that are most exposed to international competition. Producer support to rice producers corresponded to 80 per cent of farm receipts, while support to producers of sheep meat, sugar and milk corresponded to 45 per cent or more. In summary, developed countries have failed to use the opportunity to implement commitments on reduction of agricultural support in a way that would have been beneficial for developing countries.

16. Recent developments appear to reinforce the trend towards replacement of highly distorting measures with other measures that also provide producers with a significant competitive edge. The ongoing discussion within EU about a proposed reform of the Common Agricultural Policy may result in a shift from direct subsidies towards programmes linked to environmental protection, food safety standards and rural development. Similarly, the proposal made by the United States Trade Representative in July 2002 focuses on reductions in trade distorting support measures, particularly export subsidies, and in tariffs. At the same time, the new United States farm bill (the Farm Security and Rural Investment Act of 2002) provides for major increases in spending on agricultural support, which are stated to be in accordance with the United States commitments under the Agreement on Agriculture, since the measures are claimed to be non-distorting or to be covered by the *de minimus* rule. However, while direct and permanent price support measures are excluded, several of the measures in the bill would be triggered by loss of income due to price falls for individual commodities. In a situation of oversupply and decreasing prices, these measures would insulate producers in the United States from market signals and could contribute to a worsening of the oversupply situation.

17. The World Trade Organization negotiations on agriculture are currently in the process of identifying the modalities that would be the basis for new concessions and commitments, which should be agreed by March 2003.[p] In this context, developing countries are of the view that special and differential treatment for developing countries under the Agreement on Agriculture should be made more effective by establishing a "development box", which would make agricultural liberalization complementary to, rather than conflictual with, their principal development needs, including (a) increasing food security; (b) enhancing viability of low-income resource-poor farmers; and (c) removing supply-side constraints to the diversification of production and exports in developing countries.

18. The difficulties faced by developing countries, particularly least developed countries, in the implementation of agreements such as the Agreement on the Application of Sanitary and Phytosanitary Measures (the SPS Agreement) and the Agreement on Trade-related Aspects of Intellectual Property Rights (the TRIPs Agreement) also create significant problems. The standards and processes (such as the Hazard Analysis Critical Control Point system) related to the SPS Agreement threaten to turn into the most important difficulties facing developing countries' agricultural exports. Concerning the TRIPs Agreement, agricultural producers in exporting countries without sufficiently developed infrastructure for intellectual property protection risk losing markets because importing firms fear that "illegally" produced or obtained seeds may have been used in production.

2. Food security in the context of the international trading system

19. In the Marrakesh Ministerial Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least Developed and Net Food-importing Developing Countries,[j] it was recognized explicitly that during implementation of the Uruguay Round agricultural trade reform programme, some least developed countries and net food-importing developing countries might experience negative effects in terms of the availability of adequate supplies of basic foodstuffs on reasonable terms and conditions, including short-term difficulties in financing normal levels of commercial imports of basic foodstuffs.[q]

20. In many of these least developed countries and net food-importing developing countries (which collectively have a population of over 1 billion people), food imports account for more than one fifth of total imports. Many policy makers from these countries fear that they will be confronted with much higher food import bills in the years to come, both because food aid will fall (following a possible decline in surplus production in OECD countries which may result from the implementation of the Uruguay Round Agreement) and will have to be replaced by commercial food imports, and because food prices will increase owing to falling export subsidies in OECD countries and more serious price effects of supply shocks as a result of falls in worldwide food stocks.

21. As the implementation of the Uruguay Round agricultural trade reform programme has been incomplete, it is impossible to determine whether liberalization leads to higher world food prices, and to greater volatility of these prices; but if it does, the food security of least developed countries and net food-importing developing countries could be compromised unless complementary measures were taken to ensure that, in the case of price shocks, these countries would be able to import sufficient food. Food imports in these countries are now (after privatization and liberalization) mostly in private hands, and the systems used by importers to finance their purchases are not sufficiently flexible to allow a rapid increase in financing from one year to the other; thus, an argument can be made for the introduction of a new multinational food financing facility.[4]

3. Minerals and metals

22. With regard to exports of mineral commodities, tariff and non-tariff barriers have limited impact on international trade. Nevertheless, there have been a relatively large number of anti-dumping cases dealing with metals. The most important recent trade measure on minerals and metals was the temporary safeguard measures introduced by the United States in March 2002, which included the imposition of tariffs of up to 30 per cent on a large number of steel products. While it is still too early to assess the results of the measures, it appears that they have had an impact mainly on finished steel products. United States imports during the first six months of 2002 fell by 8 per cent compared with the same period in 2001.[5] Most of the decline took place in March to May. On the other hand, imports of semi-finished products, which were subject to a tariff-free quota, increased sharply. Since several countries, including most developing countries members of the World Trade Organization, were exempted from the new tariffs, and since a large number of individual exemptions have been granted, the outcomes for different exporters vary. Among developing countries, Brazil, China, the Republic of Korea and Taiwan Province of China have suffered the largest declines in finished steel exports to the United States. The long-term impacts, particularly on the oversupply situation in the world steel industry, are uncertain.

B. Market structures and the international commodity economy

23. Earlier, agricultural producers in most countries were to a large extent shielded from the world market, through measures such as tariff barriers, subsidies and stabilization funds. Such supports now survive mainly in OECD countries. In many cases, such government programmes in developing countries were not only costly but actually led to lower, albeit stable, prices for producers.[1] However, the current liberalized system has its problems. Many support structures in developing countries (for example, for contract enforcement, inspection services, marketing or finance) remain very weak years after the abolition of State marketing boards, saddling producers in these countries with a disadvantage compared with developed-country producers. The past years have also seen the virtual disappearance of local exporting companies and even local traders or distributors in many countries, and their replacement by agents or subsidiaries of international trading houses. Local service providers such as insurance companies, banks and collateral managers have also lost much of their business to foreign competition.

24. For many firms, direct investment has become less important as a tool for controlling the marketing chain, and has been replaced by production contracts, alliances and other mechanisms coordinating input suppliers, farmers, processors and traders.

25. Improved access to and use of information can to some extent offset the negative impact of increasing market concentration. Improved telecommunications, including the Internet, have led to major improvements in the generation and distribution of commodity information. For example, operating a successful

commodity exchange is no longer the reserve of major developed-country enterprises. Moreover, local portals for trading commodities can be created for developing-country users, and can reach down into the countryside, in the process revolutionizing opportunities and prospects for individual farmers with the necessary means." As information and marketing services can be combined to enhance commodity finance mechanisms, potential benefits are considerable. On the other hand, many producers may be at risk of being left further behind.

26. As the margins on traditional port-to-port trading disappeared owing to improvements in the dissemination of price information, trading houses were forced to move into local procurement, processing and distribution in developing countries. This implied greater risks, and only a few were able to thrive in this new environment. Nevertheless, the real profits in the commodity chain do not seem to lie mainly with the trading houses, however large they may be. Rather, they lie with those that control critical points along the value chain, own established brand names or have access to shelf space in supermarkets.

27. The rapid growth of supermarkets, facilitated by liberalization, has been given little attention by Governments and development agencies. In Latin America, supermarkets now account for 60 per cent of total food retailing; and the value of fruits and vegetables sold through them is two to three times as high as that exported. Supermarkets have their own modus operandi and, given their huge presence in the market, they have a definite impact on producers and production requirements in terms of cost, quality and food safety, product variety and innovation, and delivery. They provide opportunities for small producers and exporters in developing countries to access wider markets but may also hinder active and effective participation in the international value chain. The world's 200 largest supermarkets and their suppliers (with annual sales of US$ 2.800 billion), through their association (CIES — The Food Business Forum), decided earlier this year on new mandatory standards for their suppliers. The impact of this move, which may simplify the situation of exporters by reducing the number of different standards, is likely to be very important and may overshadow whatever Governments decide in the context of the World Trade Organization agreements. Moreover, to simplify operations, most supermarkets are now cutting drastically the number of their suppliers. Those left out will have to sell in a shrinking and low-priced market or find a niche market. In this environment, efforts to promote new or better production of particular commodities by, say, cooperatives need to be closely coordinated with the buying agents of supermarkets and other major end-users.

28. Consumers, particularly of agricultural commodities but to a large extent also of metals, are increasingly exigent with respect to the quality of the commodities they buy, the timeliness of delivery, origin and traceability, and the environmental and social conditions under which they have been produced. The role played by fair-trade labelling and other socially or environmentally responsible market practices is also becoming important. Many commodities are, in effect, differentiated, with tailored supply chains created to control the commodity from production to delivery to the consumer.

29. In some cases, producers benefit from this change by obtaining a price superior to the world market price; but in many cases, premium prices offered for certain commodities do not translate into better prices for producers. In many developing countries, quality control systems have not kept pace with industry requirements. For instance, one of the desirable aspects of cocoa beans is the viscosity of the resulting chocolate, for coating ice creams and the like. While manufacturers are willing to pay high prices for cocoa beans that meet the requirements, these characteristics are not even measured in many producing countries.

C. Commodity-based development and diversification

30. In several commodity-dependent developing countries, particularly least developed countries, the commodity sector, which carries the burden for the generation of savings and foreign exchange necessary for development, has not functioned as an engine of growth and industrialization. These countries are characterized by a low-productivity, low value-added and weakly competitive commodity sector, generally concentrated on a narrow range of products with weak demand growth and declining real prices. Their dependence on commodities is associated with slow export growth, which, together with terms-of-trade shocks such as those currently experienced by coffee and cotton producing countries, leads to continued low

productivity, investment and savings. Owing to slow export growth, most of these countries face foreign exchange shortages. Import volumes are low, and low levels of technology imports and lack of complementary imports result in reduced levels of investment, reduced efficiency in resource use and inefficient production processes.

31. Support from the international community and domestic reform actions are both necessary if low-income countries are to escape from the "poverty trap" imposed by commodity-dependence. In order for the commodity sector to generate the income needed for development:

- Producers and exporters must have access to timely and accurate market information, including information on prices, export markets, quality requirements and standards.
- Producers need to have access to technology that allows them to produce at a competitive cost.
- Enterprises must be able to access finance on reasonable terms and to protect themselves against price and other risks through appropriate instruments. This requires a functioning and sufficiently sophisticated banking and insurance system, as well as an appropriate regulatory framework.
- Physical infrastructure and transportation services must be available and competitively priced. This is particularly important for products such as fresh fruit and vegetables.
- Exporters need to have access to markets on non-discriminatory terms and competition from subsidized producers has to be eliminated.
- Producers and exporters must seek means for market entry, for instance, through partnering arrangements with importers or with major distributors.
- Producers must be able to meet official quality and phytosanitary standards, including for labelling and packaging, as well as unofficial standards established by buyers.

32. These issues have all been addressed in the context of an interregional project on diversification and commodity-based development undertaken by UNCTAD under the United Nations Development Account. Under that project, a number of regional and national workshops have been held, resulting in concrete proposals for action by concerned Governments, the private sector, civil society and the international community.[v]

33. In most countries that have been successful in their development efforts, the commodity sector has undergone a dynamic transformation. Through elimination of bottlenecks and adoption of appropriate strategies at the governmental and enterprise levels, competitiveness has been enhanced and hitherto unrealized areas of comparative advantage have been identified. Production patterns have changed towards higher-valued and processed products with higher growth in domestic and international demand. Specializing in these products while seeking to graduate to those generating even better returns has been the essence of successful diversification processes. Successful countries have been able to increase the value added retained in the country and have been able to plough this into investments for further development and poverty reduction. In the process, diversifying enterprises have positioned themselves in global value chains. They have adopted modern business strategies, taken calculated risks and moved to new areas with greater profitability.

34. When viewed from this perspective, diversification not only generates more resources and leads to a reduction in vulnerability to external shocks, but also entails a change in business mentality. This change is a precondition for successful diversification and also an important factor generating further development. The ability to shift production and exports from customary products to more dynamic ones without losing the expertise obtained in the former is a crucial ingredient for breaking the vicious cycle of dependence and turning it into a virtuous cycle of dynamism and development.

III. Recent developments in international cooperation on commodities

35. There are currently 24 international commodity organizations functioning at the intergovernmental level, of which six are international commodity agreements (ICAs) (on cocoa, coffee, grains, olive oil and table olives, sugar, and tropical timber) and the others are intergovernmental commodity institutions of

other types. All 24 organizations are accepted by CFC as international commodity bodies (ICBs) with regard to the preparation, submission and supervision of projects financed through its Second Account."

36. None of the existing ICAs is currently attempting to regulate the market of the commodity in question by such means as buffer stock, supply management schemes or price support measures.[x] The last agreement of that kind, the International Natural Rubber Agreement, terminated its activities in 1999, and its statistical and developmental functions were transferred to the International Rubber Study Group. The ICBs gather and disseminate information, promote research and studies on the economics of production, and the consumption and distribution of commodities, and encourage development projects.

37. A new International Cocoa Agreement was negotiated in February 2001 and is due to come into force in 2002. The 2001 Agreement is intended to help small cocoa farmers and contribute to environmental protection through "the sustainable management of cocoa resources in order to provide fair economic returns to all stakeholders in the cocoa economy". Particularly noteworthy is the emphasis on the role of the private sector in supporting a sustainable cocoa economy and in promoting cocoa consumption.

38. The International Coffee Agreement, 2001, entered into force provisionally in October 2001. It contains a number of new objectives: encouraging members to develop a sustainable coffee economy; promoting coffee consumption; promoting quality; promoting training and information programmes designed to assist the transfer of technology to member countries; and analysing and advising on preparation of projects benefiting the world coffee economy.

39. The United Nations Conference on Jute and Jute Products, 2001, negotiated an Agreement Establishing the Terms of Reference of the International Jute Study Group (IJSG) to replace the previous Agreement. IJSG was inaugurated in April 2002.

40. The bulk of development projects for commodity-dependent developing countries is financed by CFC. By May 2002 CFC had approved 105 regular projects and 37 Fast Track projects with an overall cost of US$ 317.5 million, of which CFC financed US$ 152.3 million. The projects cover 36 commodities (33 agricultural and 3 mineral).

IV. Conclusions

41. Two major problems in the area of commodities require the urgent attention of the international community: the catastrophic price falls for some commodities, particularly coffee, cotton and sugar, and the continuation of agricultural support policies by developed countries. These two problems combined represent losses to developing commodity producing countries comparable in magnitude with what all developing countries receive in official development assistance (ODA). In the long term, developing countries need assistance in order to improve their supply capacities and participation in international value chains.

42. The oversupply leading to the dramatic price falls has to be eliminated. However, it is not possible for producing countries alone to reduce the excess supply by an amount that would be sufficient to reverse the price trend, particularly in a situation where their financial resources are being exhausted as a result of these price falls. The international community should mobilize resources to finance the withdrawal of productive capacity, particularly that of high-cost producers, and economic rehabilitation, diversification and transformation in the countries concerned. To prevent similar disastrous situations, systems for compensatory financing of export shortfalls should be revisited with a view to providing a temporary safety net for developing-country producers that are heavily dependent on the export of a few commodities. In the short term, and as a minimum, support schemes to developed-country producers competing with developing-country producers of the commodities concerned, such as cotton and sugar, should be radically reduced, if not eliminated.

43. Measures also have to be taken to improve the access of developing-country agricultural exports to developed-country markets. Significant improvements in market access will require, apart from a sharp and meaningful reduction of subsidies, much deeper cuts in tariffs, or large increases in the volumes admitted at lower tariffs, preferably both. Elimination of other trade barriers and trade-distorting practices is also important. Other issues that need to be addressed in the context of further liberalization of world trade include the potential

for State trading enterprises to distort trade, the market power of large companies, the growing use of anti-dumping duties, and the possible misuse of food aid and export credits. The burden of liberalization on net food-importing countries and specialized exporters that depend on one or two key commodities also needs to be addressed.

44. **In international trade negotiations, flexibility should be provided for the most vulnerable developing countries such as least developed countries and single commodity exporters to decide what products would be subject to commitments on tariff reductions and non-tariff measures, the content of commitments and rules and disciplines. The specific measures should also take account of special difficulties faced by commodity-dependent developing countries such as depressed commodity prices and price volatility. Better conditions for transfer of technology and the design of rules (similar to those that apply to State trading enterprises) for private corporations with huge market power are among measures to be considered. Trade-related technical assistance, which appears to be an accepted commitment by developed countries, should aim not only at the negotiation or implementation of World Trade Organization agreements but also at supporting diversification efforts and developing supply capacities for benefiting from opportunities offered by the new trading framework. Improved technical and financial assistance for ensuring traceability and meeting SPS and technical barriers to trade-related standards, and for TRIPs compliance, is also among the most important needs of developing countries.**

45. **In the commodity exporting developing countries themselves, institutional factors such as insufficient market information, lack of access to technology and inputs, lack of extension services, difficult access to finance, and lack of organization and cooperation among domestic firms pose formidable barriers to the expansion of earnings from commodity exports and to diversification. In addition to efforts to improve infrastructure and strengthen farmers' and exporters' associations, it is important to improve access to market information, enhance skills and knowledge, including on financial matters, and improve legal frameworks.**

46. **Policy action in these areas, by individual Governments and the international community, with the active involvement of the private sector, can make a significant positive impact on the livelihood of developing-country commodity producers. International producer-consumer cooperation should be supported and the activities of the Second Account of the Common Fund for Commodities should be expanded. Increased funding should be made available to the Common Fund to finance research and development and extension services in developing countries as well as adaptive research on production and processing aimed particularly at smallholders and small and medium-sized enterprises in developing countries.**

Notes

[a] Statistical tables will be made available on the following web site: http://www.unctad.org/infocomm/comm_docs/docs/gapaper/index.htm.

[b] Deflated by the unit value index of manufactured goods exported by developed market economy countries.

[c] The smaller fall in real terms reflects the appreciation of the United States dollar vis-à-vis the currencies of other developed countries.

[d] "The United States sugar industry is heavily subsidized, with about half of sugar producers' revenues coming from government support ... On average, United States sugar producers have received 2.6 times the world market price for sugar since the mid-1980s." (World Bank, *Global Economic Prospects, 2002* (Washington, D.C., 2002), p. 48.

[e] Oxfam, *The Coffee Market: A Background Study* (Oxford, January 2001).

[f] ICAC, *Cotton: Review of the World Situation*, vol. 55, No. 4 (March-April 2002), p. 15.

[g] ICO, "The global coffee crisis: international cooperation to redress the situation", aide-memoire, July 2002.

[h] *Financial Times*, 17 January 2002.

[i] For instance, prices of chocolate in Switzerland increased by 4.8 per cent from May 2001 through May 2002 (Office fédéral de statistique, communiqué de presse, Neuchâtel, Switzerland, 31 May 2002). According to the Swiss chocolate industry, the price is expected to increase further in October of this year.

[j] See *Legal Instruments Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, done at Marrakesh on 15 April 1994* (GATT secretarial publication, Sales No. GATT/1994-7).

[k] J. Brooks and C. Cahill, "Why agricultural trade liberalization matters", *OECD Observer* (26 October 2001), p. 44.

[l] UNCTAD and the Commonwealth Secretariat, "Duty and quota free market access for LDCs: an analysis of Quad initiatives" (UNCTAD/DITC/TAB/Misc. 7), London and Geneva, 2001.

[m] Of the 25 members of the World Trade Organization that reserved the right to use export subsidies under the Agreement on Agriculture, 23 were developed countries. Most developing countries do not have the financial resources needed for such subsidies.

[n] It should be noted that export subsidies may be replaced by export credit guarantees which, while possibly less distorting, reduce the risk exposure of exporters. The United States increased its spending on export credit guarantees by 5 per cent in 2001 (OECD, *Agricultural Policies in OECD countries: Monitoring and Evaluation* (Paris, 2002)).

[o] TSE includes consumer support in the form of higher prices. The protection of domestic markets is of course a precondition for this support.

[p] For a detailed description of the current and planned process of negotiations on agriculture in the World Trade Organization, see the report by UNCTAD to the General Assembly on developments in the international trading system (A/57/376).

[q] See the decision of 14 November 2001 adopted by the Ministerial Conference of the World Trade Organization at its fourth session (WT/MIN/(01)/17) on implementation-related issues and concerns, para. 2.2.

[r] World Trade Organization, "Report of the Inter-Agency Panel on short-term difficulties in financing normal levels of commercial imports of basic foodstuffs" (WT/CG/62), 28 June 2002.

[s] *Metal Bulletin*, 15 August 2002, p. 17.

[t] It should be noted that tariff barriers are still often high in developing countries.

[u] For instance, Café Britt sells coffee to consumers using its 800 number, through which consumers can order bags of coffee beans directly from a farm in, say, Brazil, and have it delivered to their doorstep ("e-commerce: Marketing tool or revenue producer", *Coffee & Tea Trade Journal*, vol. 172, No. 6 (June/July 2000)).

[v] Papers presented at the workshops and recommendations can be found at: http://www.unctad.org/infocomm/Diversification/index.htm.

[w] The full list of ICBs with connections to their web sites can be found at: http://www.unctad.org/commodities/partners.htm.

[x] Such schemes are now mostly discussed in the framework of producers' arrangements, rather than in producer-consumer bodies.